

Statewide Health Care Insurance Plan Task Force

Health Insurance Administration Costs

Arizona Health Care Cost Containment System

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Summary of Health Insurance Administration

Health insurance administration covers a wide variety of activities. Typical administrative functions include:

- claims processing,
- network development and maintenance,
- case management,
- actuarial services,
- medical management,
- data collection and analysis,
- marketing, and
- administrative management.

The mix of these activities varies significantly for different types of health insurance and often by insurance carrier. Many of these activities (e.g., utilization review and case management) are designed to coordinate care among providers, as well as reduce medical expenditures. In general, insurance carriers that spend more on such activities offset the extra administrative costs by reductions in medical expenditures. However, insurance plans vary significantly in their use of such practices with varying success/failure rates.

Because certain functions of health insurance administration require specific skills, it is common for insurance plans to outsource such functions. Pharmacy benefit management companies and third-party claims administrators are common examples.

Administrative Expenditures

The level of expenditures of administration is dependent upon several factors:

- Breadth of services offered—Insurance plans with extensive medical management functions would naturally spend more than plans that do not offer such services.
- Special needs of the population—While several plans may offer case management services, a plan whose membership consists of elderly individuals with long-term care needs would spend considerably more on case management than a plan who covers primarily healthy children.
- Size of the plan may affect its per member administrative expenditures—Because there are certain fixed costs (e.g., rent, information systems) that a plan must incur independent of its enrollment, there are economies of scale that benefit large insurance plans.
- Outside requirements may impact administration expenditures—For example, Medicaid HMOs are often required to collect and submit more data to the states than commercial HMOs submit to employers.
- Efficiency in administering a health plan can vary significantly from plan to plan—Experienced personnel, data systems, cooperative practitioners, carrier-specific procedures, and related variables can significantly affect the administrative expenditures.

Administration expenditures have continued to rise in recent years. However, they have decreased as a percent of the total medical and administrative expenditures. This is due to the fact that medical expenditures have increased at much higher rates than administrative costs. Recent spending on improved information systems (e.g., Internet databases) has been significant, but it is still too early to tell if these new systems will decrease administrative or medical expenditures in the future.

As alluded to earlier, administrative expenditures vary by plan type. The table below summarizes the percentage of total expenditures spent on administration for several insurance plan types in 2000.

Plan Type	Admin Expenditures (on a per employee per month basis)	Admin Ranges as a Percent of Total Expenditures *
Indemnity	\$19	12% to 18%
PPO	\$21	12% to 18%
POS	\$28	12% to 20%
HMO (commercial)	\$21	14% to 18%
HMO (Medicaid)	\$21	10% to 21%

* The administrative ranges were calculated based on regional low and high costs of the average plan cost per employee in 2000 from the Mercer/Foster Higgins National Survey of Employer Sponsored Health Plans. The low and high costs were both divided by 2.7 (an actuarially sound figure that determines average number of people per household per employee plan) to bring the costs to an employee-only figure. The administrative expenditures were multiplied by 12 to be brought to an annual basis. This new annual figure was then divided by the employee-only costs to calculate the administrative ranges represented above.

Additional Resources:

National Survey of Employer-Sponsored Health Plans, Mercer/Foster Higgins, 2000.

Sherlock Expense Evaluation Reports (SEER), Published by Sherlock Company 2001.

The InterStudy Competitive Edge, Part II: HMO Industry Report, Published by Mercer's WRG 2000.